

Demonetization needs a Devil's Advocate

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OPINION | Demonetization needs a Devil's Advocate

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By Arjun Sreekumar



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Five months into demonetization, reporting interest on the topic has waned and the cacophony on how the policy measure was a burden has died down. Those following demonetization would've noticed that a positive report on the topic was a diamond in the rough whilst critique was borderline superfluous. Without the doubt, many negatives highlighted in these reports were relevant, but a fallacy in the majority of them was that demonetization was dissected as a stand-alone policy measure when in actuality it is not. Demonetization should be assessed through a prism of interconnected financial policies, affirmative action, and possible macroeconomic implications to make a stronger judgment call. Also, the analysis of the measure should be done *vis-à-vis* the objectives it set out to attain – eradicating black money, finding tax defaulters, counterfeit currency and providing ancillary stimulus to the nation's economy.

Most sources peg the amount of black money in India between \$ 44 and \$76 Billion. We need to put the quantum of this money in perspective. The budget of two of the most important social security measures – the **National Food Security Act 2013** and **MGNREGA** is rough \$ 30 Billion, less than half of the highest projected amount of black money. Just imagine how much the nation's social security budget can grow even if a fraction of this is reintegrated into the economy. Demonetization invalidated hoards of currency stocked by tax evaders. Many of these erring individuals had only one way to legitimize the hoarded cash – the Pradhan Mantri Garib Kalyan Yojana, an income declaration scheme the government introduced about a month after the demonetization exercise. Though the total amount collected under the income declaration scheme is not officially out, the penalties and taxes collected will form a significant chunk that the government can direct towards affirmative action that will lift people out of poverty and better health outcomes of the marginalized. Also, from a macroeconomic perspective, the income generated from the government through this may have positive ramifications on the nation's fiscal deficit which in turn improves India's borrowing power from global institutions. More credit is thus available for developmental measures in the long term. Domino effects of the demonetization such as these are clandestine, but many.

Demonetization pushed invalidated currency to be invested in bank accounts. This proved to be greatly beneficial in two ways. There have been many instances in the past where banks collude with clients to help convert black money into white. The Enforcement Directorate has started analyzing deposit patterns that happened post demonetization to identify banks which may have been involved in hawala transactions and money laundering. Inquiries are being conducted in at least 50 banks and probes are being conducted by the IT department, CBI and ED to identify and prosecute law-breakers. The trove of data yielded by the exercise is also being used to identify probable tax evaders by tracking account activity.

The second benefit from the cash inflow is that **\$32 Billion has been deposited** into bank accounts within 50 days post demonetization. Money locked away in vaults and hidden in safe places for years has been finally brought into circulation and is part of the formal economy now. Banks are flush with cash as a result of which interest rates have been lowered. The loans disbursed is poised to grow and the borrower does not feel the pinch of a high-interest rate. This will be a boon for many – the budding entrepreneur who needs funding to grow his venture, the manufacturing plant owner who needs liquidity infusion to build inventory and the farmer facing the setbacks of a bad crop season among others. Infrastructure, manufacturing, agriculture and services will thus have access to more funding indirectly having positive ramifications vis a vis job creation, GDP growth, FDI and increased foreign exchange reserves.

Demonetization is also latently in concert with other government schemes and policies such as Start Up India, Stand Up India indicating a well thought out plan of action rather than an abrupt move. The move has also given a boost to the digital economy driving sales across many new start-ups. More importantly, it has instigated a behavioral change in many to go cashless, **activate idle Pradhan Mantri Jan Dhan Yojana accounts** and master digital payments. Many beneficiaries of social security assistance are more amenable to monetary benefits being directly transferred to their accounts now, thus cutting down middlemen. There's a dual advantage here. The beneficiary gets the amount that was really due to him without pilferage and the government saves on distribution costs, thereby increasing the quantum of money available for social security schemes. This mutually reinforcing relationship is a consequence of demonetization.

And, of course, there is the security aspect of the move. For a nation like **India which is ranked 8th on the Global Terrorism Index 2016**, demonetization delivers an uppercut to terrorist/ Maoist funding. Millions of dollars worth of currency from sources such as extortion, "protection money", arms dealing and drug trafficking are rendered worthless. Annually, seven billion Fake Indian Currency Notes (FICN) are pumped into the economy (mostly originating from Pakistan). Crores of FICN are rendered useless. Demonetization was a coup de grace against nonstate anti-national organizations, these cash-rich organizations reduced to a state of penury in a master stroke.

Without a doubt, the move has caused the public a lot of inconveniences. But we should not let ourselves be led by anecdotal evidence and political biases, the issue must be dissected by understanding the many interconnections in play – social, economic and security oriented. It is only then that the big picture starts to materialize - the picture of a strong economy, an equitable nation, and a leading industry. Citizens have to be patient to reap the rewards. It's as the old axiom follows – Rome was not built in a day.

About the Author:

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